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NOT TO BE PUBLISHED IN THE OFFICIAL REPORTS

IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

SECOND APPELLATE DISTRICT

DIVISION ONE

DAVID DIAZ et al., Plaintiffs and Respondents, v. GEORGE AJRAB et al., Defendants and Appellants.	B203081 (Los Angeles County Super. Ct. No. NC035141)

APPEAL from a judgment of the Superior Court of Los Angeles County. Patrick T. Madden, Judge. Reversed and remanded

Smyth Law Office, Andrew E. Smyth; Benedon & Serlin, Gerald M. Serlin and Kelly R. Horwitz for Defendant and Appellant George Ajrab.

Law Office of Stephen A. Colby and Stephen A. Colby for Plaintiffs and Respondents.

David and Linda Diaz purchased an apartment complex from George Ajrab. During escrow, Ajrab promised the Diazes he would assign to them his position in a second escrow on one of the units, so that they would own the entire complex. There was, however, no second escrow on the unit, and the Diazes ended up owning only 19 of the 20 units in the complex. They sued Ajrab for fraud and breach of contract, and after trial the court awarded the Diazes compensatory and punitive damages, as well as attorney fees and costs. Ajrab appeals, arguing that the Diazes were on inquiry notice that there was no escrow on the unit, and that the court used the wrong measure of damages. We agree with the trial court that the Diazes were not on inquiry notice of Ajrab's deceit. However, we must reverse the award of compensatory and punitive damages. Under the facts of this case and the applicable statutes, the Diazes are not entitled to monetary damages.

BACKGROUND

Ajrab owned an apartment complex at 1133 Pine Avenue in Long Beach.[1] The three buildings contained 20 units, which were numbered 1-12 and 15-22. Ajrab listed the complex for sale for $769,000 in February 2002, representing that he owned 18 units. Three months later, when he had received no offers for the 18 units, he changed the listing to reflect that all 20 units were for sale, asking $855,000.

The Diazes wanted to buy a rental property. Their agent, Clement Lombardi of Century 21 Beachside Realty,[2] brought Ajrab's 20-unit listing to their attention, and they entered into negotiations with Ajrab's real estate agent, Michael Lembeck. The parties

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[1] Ajrab's mother, Egenie Ajrab, was the owner of record of the apartment complex. Ajrab acted as his mother's attorney-in-fact, under a written power of attorney. The parties stipulated that Ajrab and his mother Egenie could be treated as alter egos in the litigation.

[2] The Diazes also named Beachside as a defendant. The court found that Beachside was not liable for any misrepresentation.

reached an agreement that the Diazes would buy all 20 units for $800,000, and they opened an escrow at Talbrook II Escrow on July 12, 2002 ("Talbrook Escrow").

The Diazes learned in a preliminary title report that Ajrab owned only 18 of the 20 units, excluding units 19 and 21. Ajrab was eventually able to secure unit 19 for delivery to the Diazes, leaving only unit 21. He told the Diazes that he had opened a second escrow at Chicago Title to purchase unit 21, and the parties agreed that Ajrab would assign his position in that second escrow to the Diazes.

The problem was that there was no escrow for unit 21 at Chicago Title. Preliminary escrow papers had been prepared, but there was no signed purchase agreement and the seller never returned signed instructions. Nevertheless, Ajrab represented to the Diazes that they could assume his position in the second escrow to buy the missing unit. He was in a hurry to sell the complex, because the City of Long Beach had cited the complex for numerous building code violations. If Ajrab did not quickly sell or repair the units, he faced jail time.

The Diazes, believing Ajrab's representation that an escrow existed for unit 21, signed an addendum which amended the purchase agreement on September 4, 2002. The amended agreement reduced the selling price by $60,000 to $740,000, and acknowledged that only 19 of the 20 units were included. The $60,000 discount was meant to allow the Diazes to buy unit 21 (through the nonexistent escrow) for $45,000, with the understanding that they would then pay Ajrab the extra $15,000 less closing costs. The addendum stated "Buyer to assume seller's position in escrow at Chicago Title for purchase of Unit 21." The Diazes also amended the escrow instructions with Talbrook to reflect the change.

The Talbrook escrow for the 19 units closed on September 18, 2002. Months later, the Diazes attempted to refinance the mortgage on the complex, but were unable to get a favorable interest rate because they owned only 19 units. The Diazes checked the status of the Chicago Title escrow and learned that there was no escrow for unit 21.

The Diazes sued Ajrab for breach of contract, fraud, declaratory relief, negligent misrepresentation, and indemnity, filing their fourth amended complaint on December 29, 2005. Ajrab sued the Diazes for breach of contract and declaratory relief (seeking the $15,000 he was due after the Diazes bought unit 21). The two lawsuits were consolidated for trial.

A court trial began September 21, 2006. The trial court issued its final written decision on June 7, 2007, finding Ajrab liable for fraud and breach of contract. The court concluded that Ajrab had intentionally misrepresented to the Diazes that he could deliver a viable position in an escrow on the final unit, leading the Diazes to continue with the transaction rather than terminate it. The court also found that Ajrab was not entitled to any recovery, because the Diazes relied on his misrepresentation when they entered into the agreement to reimburse Ajrab $15,000.[3] The trial court awarded the Diazes $85,000 in compensatory damages (the difference between the $60,000 price reduction reflecting the absence of unit 21 and the $145,000 it would cost the Diazes to purchase unit 21 as of the time of trial), $100,000 in punitive damages, contractual attorney fees, and costs.

ANALYSIS

I. The Diazes were not on inquiry notice that there was no escrow on unit 21.

Ajrab argues that Lombardi, the Diazes' real estate agent, and through Lombardi the Diazes themselves, were put on inquiry notice that there was no escrow at Chicago Title for unit 21. He contends that because the Diazes were on inquiry notice, they were charged with all the information regarding the second escrow for unit 21, and therefore he could not be liable for misrepresenting to the Diazes that an escrow existed.

Chicago Title escrow officer Ann Toney testified that on August 19, 2002 she faxed assignment papers to Lombardi, along with unsigned escrow instructions for unit 21. Lombardi denied seeing the faxed instructions. The court found, however, that

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[3] Ajrab does not appeal from that decision.

Lombardi had provided Toney with information about the Diazes so she could prepare the assignment, and that Toney had then transmitted the assignment paperwork and the unsigned escrow instructions to Lombardi.

Inquiry notice is "'[N]otice attributed to a person when the information would lead an ordinarily prudent person to investigate the matter further.'" . . . [T]he concept of inquiry notice applies only where the plaintiff does not already have actual notice of the facts supporting his cause of action." (*Amtower v. Photon Dynamics, Inc.* (2008) 158 Cal.App.4th 1582, 1601.) Ajrab does not argue that Lombardi had actual notice that there was no escrow. He contends that the receipt of the unsigned escrow instructions with the assignment papers was information that charged Lombardi, and through him the Diazes, with inquiry notice, requiring the Diazes to investigate further to determine whether there actually was an escrow for unit 21.

Lombardi had information that escrow instructions had been drawn up for unit 21 and that they had not been signed. We may impute to the Diazes their agent's knowledge that the instructions had not yet been signed, and to that extent the Diazes were on inquiry notice. (See *Lucas v. Pollock* (1992) 7 Cal.App.4th 668, 673 [real estate agent's knowledge acquired in the course of his agency is imputed as knowledge of principal].)

But we cannot charge the Diazes with constructive knowledge of any additional information, because they were not a party to the second escrow. "'[A]ll parties to an escrow have the legal right to examine all the papers deposited in the escrow. . . . *When there are two escrows, the doctrine of imputed knowledge has no application to documents deposited in the escrow to which the party sought to be charged with notice was not a participant.*'" (*Far West Savings and Loan Assn. v. McLaughlin* (1988) 201 Cal.App.3d 67, 74-75.) The Diazes were not participants in the purported second escrow between Ajrab and the owner of unit 21, and therefore they had no legal right to examine the escrow papers. They cannot be held responsible for not investigating further into a private transaction between third parties. The Diazes did not have constructive knowledge that no purchase agreement had been signed and that the escrow was a sham.

Ajrab cites *In re Marriage of Cloney* (2001) 91 Cal.App.4th 429, in which a buyer's escrow agent's actual knowledge of the true name of the seller was imputed to the buyer, placing the buyer on inquiry notice of possible title problems. Because the seller's divorce judgment was recorded under his true name, the court concluded that applicable statutes imposed constructive knowledge of the existence of a judgment lien (related to the divorce) on the buyer. (*Id*. at p. 442.) Here, by contrast, Toney was not the Diazes' escrow agent, and so the Diazes did not have constructive knowledge of any facts regarding the escrow beyond the instructions transmitted to their agent, Lombardi.

After the unsigned escrow instructions were transmitted to Lombardi on August 19, 2002, and up to and including the close of the Talbrook escrow on September 18, 2002, Ajrab continued to represent to the Diazes that he would assign them his position in the nonexistent escrow. The Diazes were entitled to rely on his continued misrepresentation, because the Diazes did not have a legal right to inspect the documentation that would prove Ajrab a liar.

The Diazes' inquiry notice did not impute to them the constructive knowledge that there was no escrow for unit 21.

II. Compensatory damages cannot be based on the value of unit 21 at the time of trial.

A. Civil Code Section 3306 governs the award of contract damages.

The trial court heard testimony from the Diazes' expert witness that the couple's total loss from not owning unit 21 was $955,000 at the time of trial. This figure included seven different measures of damages, including the loss of standard refinancing, the decreased value of the complex without unit 21 (at the time of trial in 2006), loss of rental income on unit 21, loss of rents on other units because of the inability to improve the partially owned complex, and the cost of buying unit 21. The expert testified that the unit was available at the time of trial for $145,000.

The trial court found that the Diazes had a duty to mitigate their damages, and "rather than incur significant consequential damages, plaintiffs are able to purchase the twentieth unit [unit 21] for $145,000. The damages for breach of contract reflect the difference between the purchase price of the last unit as of the time of trial ($145,000) and the $60,000 already paid to Mr. and Mrs. Diaz by Mr. Ajrab for the purchase of unit 21. Thus, plaintiff's damages are $85,000." The court awarded the $85,000 as compensatory damages for breach of contract and found that the damages for fraud were also $85,000. Because there could be no double recovery, the court awarded $85,000 as the total award of compensatory damages.

Ajrab correctly argues that damages should have been based upon the value of the property at the time of breach, not at the time of trial. Civil Code section 3306 provides: "The detriment caused by the breach of an agreement to convey an estate in real property, is deemed to be the price paid, and the expenses properly incurred in examining the title and preparing the necessary papers, *the difference between the price agreed to be paid and the value of the estate agreed to be conveyed at the time of the breach,* the expenses properly incurred in preparing to enter upon the land, consequential damages according to proof, and interest." (Italics added.) Section 3306 therefore provides only for "'loss-of-bargain damages' measured by the difference between the contract price and the fair market value on the date of the breach." (*Reese v. Wong* (2001) 93 Cal.App.4th 51, 56.) It is improper to measure consequential damages by "the appreciation in value of property from the time of the breach to the time of trial," because under that theory "contract damages would be dependent not on the reasonable expectations of the parties at the time of their contracts, but on the fluctuations in the real estate market, the existence of congestion in the calendars of trial courts, and the success of the parties in delaying or advancing trial dates, depending on which tactic was to their advantage." (*Id.* at pp. 59, 61.)

Ajrab points out that the Diazes received a credit of $60,000 for unit 21. The only evidence at trial was that the parties thought unit 21 was worth $45,000 at the time of this transaction; there certainly was no evidence that it had a market value of more than

$60,000. Measuring, as we must, the damages by the difference in value of the agreed-upon price and the actual value at the time of the breach, it appears that the Diazes are not due any compensatory damages under section 3306. They certainly are not due the extra $85,000 required to buy the unit at the time of trial.[4] Whether or not this is "unfair under the circumstances . . . our limited role in interpreting statutes is to follow the Legislature's intent as exhibited by the plain meaning of the actual words of the statutes. [Citation.] Section 3306 does not authorize damages based on the value of property at the time of trial, and we are not authorized to rewrite that statute or insert qualifying provisions not included by the Legislature." (*Reese v. Wong*, *supra*, 93 Cal.App.4th at p. 61.)

The Diazes attempt to avoid the application of section 3306 by characterizing their claim as alleging the breach of a collateral promise ("the obligation to assign an operative escrow") rather than of an agreement to convey real property. But their complaint alleges that Ajrab breached a "written agreement with [the Diazes] to sell all twenty (20) Apartments." After the parties agreed to amend the purchase agreement and the escrow instructions, reducing the purchase price by $60,000 and assigning Ajrab's position in the escrow for unit 21 to the Diazes, "Ajrab . . . failed to transfer or convey the entire 20 units," and thereby "failed . . . to comply with the terms and conditions of the written Purchase Contract and/or Escrow Instructions." The alleged breach is a breach of the purchase agreement's promise to convey all 20 units of the complex, and section 3306 controls the damage award.[5]

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[4] The Diazes presented no evidence of the fair market value of the entire complex with and without unit 21 at the time of the breach of contract.

[5] As the court stated in *Coger v. Wiltsey* (1931) 117 Cal.App. 652, 657: "The position of respondent is that 'Section 3306 of the Civil Code, referred to by counsel, refers only to breach of agreement to convey estate in real property. This is an agreement to make an escrow.' We must confess that we are unable to follow counsel in his view. The provision for an escrow was one of the terms of the agreement to convey, and a breach thereof was a breach of the agreement, and the sole and exclusive remedy therefor is found in the Code section referred to."

On their contract claim, the Diazes may recover only the difference between what they paid for the complex and the complex's fair market value at the time of the breach. They presented no evidence at trial establishing the fair market value of the entire complex with and without unit 21 *at the time of the breach of contract*. Instead, the only evidence was that the *single* unit was valued at $45,000 and the Diazes received a $60,000 credit to allow them to purchase the unit and cover costs.

The parties prescribed their own solution to the absence of unit 21 and made their own estimate of its value. If their guess proved inaccurate, the Diazes had the right to prove that they were damaged in an amount larger than $45,000 at the time of the breach. They failed to take this opportunity. They instead proposed a fanciful loss of $955,000, which the trial court correctly found to be avoidable and unreasonable. The Diazes proved no proper contract damages under section 3306.

B. Civil Code section 3343 governs the award of damages for fraud.

A similar limitation applies to the damages available on the Diazes' fraud claim. "There are two measures of damages for fraud: out-of-pocket and benefit-of-the-bargain. The out-of-pocket measure restores a plaintiff to the financial position he enjoyed prior to the fraudulent transaction, awarding the difference in actual value between what the plaintiff gave and what he received. The benefit-of-the-bargain measure places a defrauded plaintiff in the position he would have enjoyed had the false representation been true, awarding him the difference in value between what he actually received and what he was fraudulently led to believe he would receive. [Citation.] [¶] 'In fraud cases involving the "purchase, sale or exchange of property," the Legislature has expressly provided that the "out-of-pocket" rather than the "benefit-of-the-bargain" measure of damages should apply.'" (*Fragale v. Faulkner* (2003) 110 Cal.App.4th 229, 236.) Civil Code section 3343, subdivision (a) provides: "One defrauded in the purchase, sale or exchange of property is entitled to recover the difference between the actual value of that with which the defrauded person parted and the actual value of that which he received . . . ." Subdivision (b) specifies that the benefit-of-the-bargain rule does not apply: "Nothing in this section shall . . . . (1) Permit the defrauded person to recover any amount

measured by the difference between the value of the property as represented and the actual value thereof." (See *OCM Principal Opportunities Fund v. CIBC World Markets Corp.* (2007) 157 Cal.App.4th 835, 870-875 [applying out-of-pocket rule to damages for fraudulent misrepresentation in sale of securities]).

The Diazes claimed they were defrauded by Ajrab in the purchase of the apartment complex when he falsely promised to assign them his escrow position in unit 21. Under section 3343, they are limited to their out-of-pocket damages, the difference in the actual value of what they gave (what they paid for the apartment complex) and the value of what they received (the apartment complex without unit 21). The court instead awarded the Diazes the same amount it had awarded for the breach of contract, $85,000. That amount transparently gives the Diazes the benefit-of-the-bargain, placing them in the position of owning unit 21 (where they would have been if Ajrab's representation that they could assume an existing escrow had been true). The $85,000 in damages for fraud cannot be justified under section 3343.

C. Because no actual damages were due for fraud, the Diazes may not recover punitive damages.

The trial court also awarded $100,000 in punitive damages on the Diazes' fraud claim, based on "evidence that Mr. Ajrab received approximately $800,000 for the sale of the nineteen units" and despite acknowledging "there was no evidence of Ajrab's total net worth." We note that "an award of punitive damages cannot be sustained on appeal unless the trial record contains meaningful evidence of the defendant's financial condition." (*Baxter v. Peterson* (2007) 150 Cal.App.4th 673, 680.) But even if the record did contain such meaningful evidence, "[a]n award of actual damages, even if nominal, is required to recover punitive damages." (*Sole Energy Co. v. Petrominerals Corp.* (2005) 128 Cal.App.4th 212, 239; see Civ. Code § 3294, subd. (a) [plaintiff may recover punitive damages "*in addition to* the actual damages"].) Because the Diazes cannot recover compensatory damages from Ajrab, they cannot recover punitive damages. (*Sole Energy Co. v. Petrominerals Corp.*, *supra*, 128 Cal.App.4th at p. 239.)

The trial court explicitly and justifiably found that Ajrab defrauded the Diazes and that Ajrab's testimony was entirely unworthy of belief. Even so, the absence of any proof of the proper measure of damages requires entry of judgment in favor of the defendant.

DISPOSITION

We reverse the award of damages to the Diazes for breach of contract and fraud and remand to the trial court for entry of judgment in favor of Ajrab. The parties shall bear their own costs on appeal.

NOT TO BE PUBLISHED.

BAUER, J.*

We concur:

MALLANO, P.J.

ROTHSCHILD, J.

* Judge of the Orange County Superior Court, assigned by the Chief Justice pursuant to article VI, section 6 of the California Constitution.